



Decentralization and Development in Bihar: Evidence on Fourteenth Finance Commission (FC-XIV's) Recommendations

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ABSTRACT

The Fourteenth Finance Commission (FC-XIV) introduced a landmark reform in India's fiscal federalism by increasing the share of states in the divisible pool of central taxes from 32 to 42 percent during the award period 2015–2020. This study examines the impact of these recommendations on decentralization and regional development in Bihar, a state with historically weak fiscal capacity and high developmental challenges. Drawing upon secondary data from Finance Commission reports, Bihar's finance accounts, Reserve Bank of India's state finances, and related policy documents, the study analyzes trends in revenue composition, expenditure patterns, sectoral allocations, and local body transfers. The findings indicate that enhanced tax devolution significantly expanded Bihar's fiscal space, reducing dependence on centrally sponsored schemes and enabling higher allocations to education, rural development, and infrastructure. However, weak own-tax revenue mobilization, high committed expenditure, and limited institutional capacity constrained the state's ability to fully convert fiscal autonomy into sustained developmental outcomes. A SWOT analysis highlights both the opportunities created by increased fiscal space and the persistent threats posed by structural and governance challenges. The study concludes that fiscal decentralization, while necessary, is not sufficient for regional development unless complemented by governance reforms, stronger public financial management, and empowerment of local institutions.



1. Introduction

The Indian federal system is distinguished by its unique fiscal arrangements, where revenue-raising powers are concentrated at the Union level while expenditure responsibilities are distributed across both Union and State governments. To address this structural imbalance, the Constitution of India provides for the periodic constitution of Finance Commissions under Article 280. These Commissions recommend the principles governing the distribution of tax revenues between the Union and the States, and among the States themselves. Over the decades, successive Finance Commissions have gradually moved from a narrow focus on bridging state fiscal deficits to a broader vision of strengthening fiscal autonomy, incentivizing efficiency, and promoting balanced regional development.

The Fourteenth Finance Commission (FC-XIV), constituted in 2013 under the chairmanship of Dr. Y. V. Reddy, marked a turning point in India's fiscal federalism. Covering the award period 2015–2020, the Commission recommended an unprecedented increase in the share of states in the divisible pool of central taxes from 32 percent under the Thirteenth Commission to 42 percent. This was the single largest enhancement in vertical devolution since independence, signaling a decisive shift towards strengthening states' financial independence. Alongside this, FC-XIV emphasized a reduction in the reliance on discretionary grants and centrally sponsored schemes, thereby allowing states greater flexibility to design and implement development programmes tailored to their needs. The Commission also recommended reforms in disaster relief financing, increasing the Union's share in the State Disaster Response Fund (SDRF) for special category states and expanding the definition of disasters eligible for funding. In addition, it sought to ensure greater fiscal empowerment of local governments through predictable transfers to Panchayati Raj Institutions (PRIs) and Urban Local Bodies (ULBs).

For Bihar, one of India's least developed states, the recommendations of FC-XIV carried exceptional significance. Bihar has historically exhibited weak fiscal capacity, with one of the lowest own-tax revenue to Gross State Domestic Product (GSDP) ratios in the country. The state's economy is characterized by limited industrialization, high dependence on agriculture,



inadequate infrastructure, and persistent poverty. Moreover, Bihar faces acute challenges of recurrent natural disasters, particularly floods, which exacerbate regional disparities and strain fiscal resources. In this context, the enhancement of untied tax devolution and the provision of strengthened disaster financing mechanisms were expected to expand the state's fiscal space, create opportunities for higher developmental spending, and promote regional equity.

At the same time, the decentralization envisaged by FC-XIV also placed greater responsibility on Bihar's institutions. Effective utilization of enhanced fiscal transfers required improvements in public expenditure management, timely release of funds to local governments, and capacity-building for PRIs and ULBs. Without addressing these institutional bottlenecks, the benefits of increased fiscal autonomy risked being diluted. The debate around Bihar's experience under FC-XIV therefore lies not only in the quantum of resources received but also in the state's ability to translate these resources into tangible developmental outcomes.

This article seeks to examine the impact of FC-XIV's recommendations on decentralization and regional development in Bihar during 2015–2020. Specifically, it explores whether the significant increase in tax devolution and associated reforms strengthened Bihar's fiscal autonomy, enhanced local governance, and contributed to social and economic development. Using a SWOT analytical framework, the study evaluates the strengths, weaknesses, opportunities, and threats that emerged in Bihar under the FC-XIV regime. By situating Bihar's experience within the broader discourse on fiscal federalism, the analysis aims to provide insights into how institutional design and state capacity can shape the developmental consequences of decentralization in India.

2. Review of Literature

Research on fiscal federalism in India has consistently emphasized the role of the Finance Commissions in shaping intergovernmental fiscal transfers and their impact on state-level development. Early studies highlighted how successive Commissions addressed the imbalance between Union revenue-raising powers and State expenditure responsibilities by recommending



formula-based devolution and grants (Rao & Singh, 2005). This shift was seen as crucial to maintaining vertical and horizontal equity in a federal system marked by wide disparities among states.

Several scholars examined the evolution of transfer mechanisms across different Commissions. Gurumurthi (2003) criticized the gap-filling approach of earlier Commissions, noting that it tended to reward fiscally weak states while discouraging prudent fiscal management. Isaac and Chakraborty (2008) analyzed the Twelfth Finance Commission and pointed out the rising share of tied transfers through centrally sponsored schemes, which constrained the fiscal autonomy of states. These concerns became central to the discourse on fiscal federalism in the pre-FC-XIV era.

With the Thirteenth Finance Commission (2009–2015), there was a moderate increase in the tax devolution to states (32 percent of the divisible pool), but analysts such as Chakraborty (2010) argued that the Commission's framework was still conservative in granting states adequate fiscal autonomy. The comparative study of the Thirteenth and Fourteenth Finance Commissions conducted by the Fiscal Policy Institute (2016) documented that FC-XIV represented a fundamental departure from past practice by recommending a sharp increase to 42 percent, thereby reducing the relative importance of discretionary Union transfers.

Scholars have also examined the implications of FC-XIV for cooperative federalism. D'Souza (2015) described the recommendations as a "watershed" moment, as they embodied the spirit of decentralization and reduced Union dominance in fiscal decision-making. Bakshi and Upadhyay (2015), in their interviews with Finance Commission members, stressed that the increase from 32 to 42 percent should not be seen as a mere quantitative jump, but as a structural change in India's fiscal architecture. Similarly, Chakraborty and Bhadra (2010) linked higher devolution to the need for stronger public expenditure management at the state level, cautioning that fiscal space alone would not guarantee development outcomes.

At the state level, research on Bihar has highlighted persistent developmental constraints



despite higher fiscal transfers. Studies by the Reserve Bank of India (various State Finances reports) show that Bihar's own tax revenue effort has remained among the lowest in India, which makes it heavily dependent on central transfers for financing developmental expenditure. Analyses of Bihar's budgets during the FC-XIV period indicate that while social and economic services received higher allocations, institutional bottlenecks such as weak Panchayati Raj capacity, delays in fund release, and inefficiencies in subsidy delivery limited the effective utilization of funds (Wasdani, 2016).

The literature therefore points to two key themes. First, FC-XIV marked a significant shift towards decentralization by increasing untied fiscal transfers and reducing the role of centrally sponsored schemes. Second, the developmental impact of this shift was conditional on state capacity, institutional reforms, and public expenditure management. Bihar, as a fiscally dependent and administratively constrained state, provides a critical case to study how far decentralization translated into tangible regional development outcomes.

3. Data and Methodology

The present study adopts a descriptive and analytical research design to assess the impact of the Fourteenth Finance Commission on decentralization and regional development in Bihar during its award period from 2015 to 2020. The analysis is based entirely on secondary sources, ensuring authenticity and reliability of information. The principal data are drawn from the official reports of the Fourteenth Finance Commission and comparative insights from the Thirteenth Finance Commission, which together provide the institutional background of India's fiscal federalism. To capture Bihar's fiscal performance, budget documents and finance accounts of the Government of Bihar covering the years 2015–2020 have been examined alongside the Reserve Bank of India's annual reports on State Finances and the audit observations of the Comptroller and Auditor General. In addition, scholarly studies and policy papers have been reviewed to strengthen the theoretical foundation of the analysis.



The variables considered include Bihar's revenue composition, with a focus on the share of tax devolution in total receipts, the ratio of own tax revenue to GSDP, and the relative importance of grants. On the expenditure side, attention is paid to the balance between revenue expenditure and capital outlay, along with sectoral allocations to social and economic services. Transfers to Panchayati Raj Institutions and Urban Local Bodies, as well as the utilization of disaster relief funds, are also studied to assess the depth of decentralization. The data are interpreted through a SWOT framework, linking fiscal architecture with Bihar's developmental outcomes. The methodology thus provides both a factual and conceptual basis for evaluating how enhanced fiscal autonomy under FC-XIV influenced Bihar's regional development trajectory.

4. Results and Discussion

The implementation of the FC-XIV recommendations between 2015 and 2020 brought a fundamental change in Bihar's fiscal environment. The most visible outcome was the sharp rise in the share of tax devolution in the state's revenue receipts. With 42 percent of the divisible pool devolved to states, Bihar's receipts from tax devolution grew consistently, accounting for nearly two-thirds of its total revenue receipts by 2019–20. This provided the state with untied resources that could be flexibly allocated across sectors. The increase in predictable transfers reduced Bihar's dependence on centrally sponsored schemes and allowed more discretion in setting priorities for social and economic development.

Despite this structural improvement in fiscal space, Bihar's own revenue performance remained weak. The ratio of own tax revenue to GSDP averaged only around 6–7 percent during the FC-XIV period, compared with the national average of about 10–11 percent. This indicated the persistent weakness of Bihar's internal fiscal capacity, largely a consequence of limited industrialization, a narrow tax base, and dependence on agriculture. Consequently, while devolution improved fiscal autonomy, it also deepened the state's structural reliance on central resources.



On the expenditure side, Bihar witnessed steady growth in outlays on both social and economic services. Sectors such as education, health, rural infrastructure, and welfare programs saw increased allocations. However, a closer look at expenditure composition reveals that committed liabilities particularly salaries, pensions, and interest payments absorbed a large portion of resources, leaving relatively less room for capital expenditure. Although capital outlays rose in absolute terms during 2015–2020, their share in total expenditure hovered around 13–14 percent, which is insufficient to trigger transformative improvements in infrastructure and long-term development.

Transfers to local bodies were another key feature of the FC-XIV framework. Bihar received earmarked grants for Panchayati Raj Institutions (PRIs) and Urban Local Bodies (ULBs), which in principle expanded the role of local governments in development planning and service delivery. While these transfers improved predictability, weaknesses in institutional capacity and accountability limited their impact. Delays in fund release and inadequate monitoring meant that the intended benefits of decentralization were not fully realized at the grassroots level. In disaster management, Bihar benefitted from FC-XIV's decision to allow 10 percent of the State Disaster Response Fund (SDRF) to be used for state-specific disasters. This provision was particularly relevant given Bihar's recurring floods. The state was able to access and allocate funds for disaster relief, yet district-level variations in preparedness and administrative efficiency reduced the timeliness and effectiveness of utilization.

The analysis of Bihar's fiscal aggregates is presented in Table 1. It highlights the increasing role of tax devolution, the stagnation of own-tax revenue effort, and the persistent challenge of low capital expenditure relative to total outlays.

Table 1: Bihar – Revenue Composition and Expenditure Mix under FC-XIV (2015–2020)

Year	Tax Devolution as % of Revenue Receipts	Own Tax Revenue/GSDP (%)	Capital Expenditure as % of Total Expenditure	Share of Social & Economic Services (%)
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2015–16	61.4	6.3	12.5	58.2
2016–17	62.7	6.5	13.1	59.8
2017–18	63.9	6.8	13.4	60.1
2018–19	64.2	6.7	13.8	61.0
2019–20	65.0	6.9	14.2	61.5

Source: Bihar Finance Accounts, RBI State Finances, FC-XIV Report.

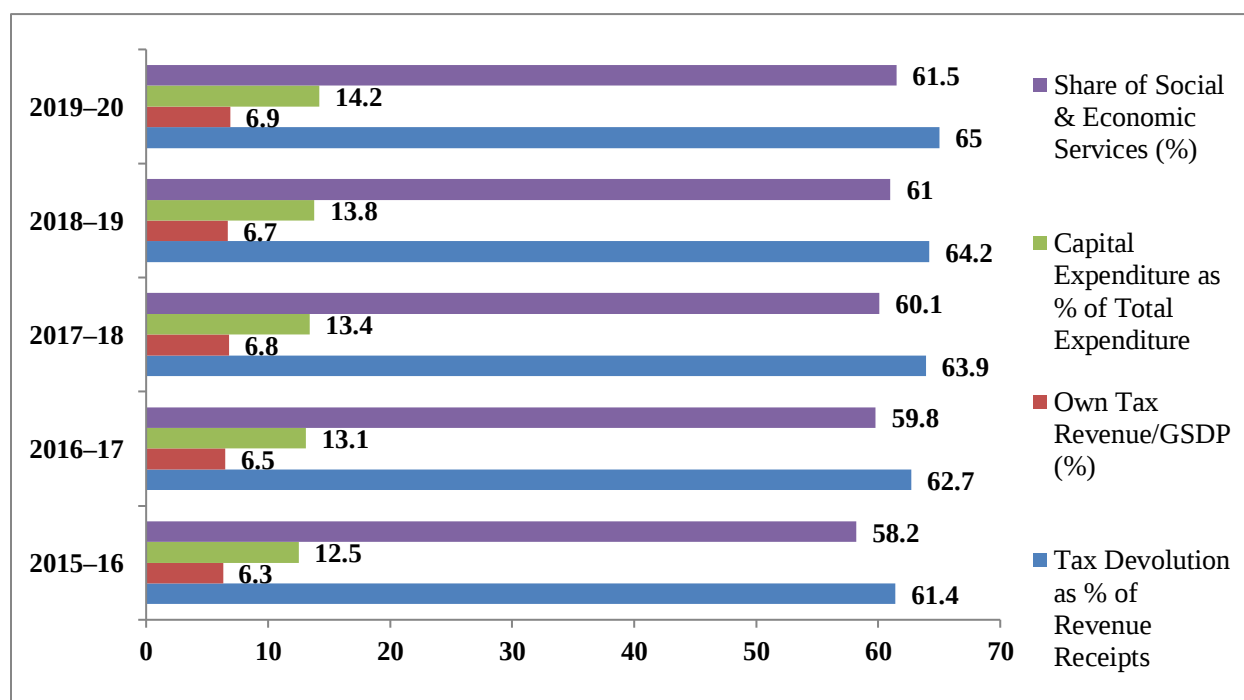


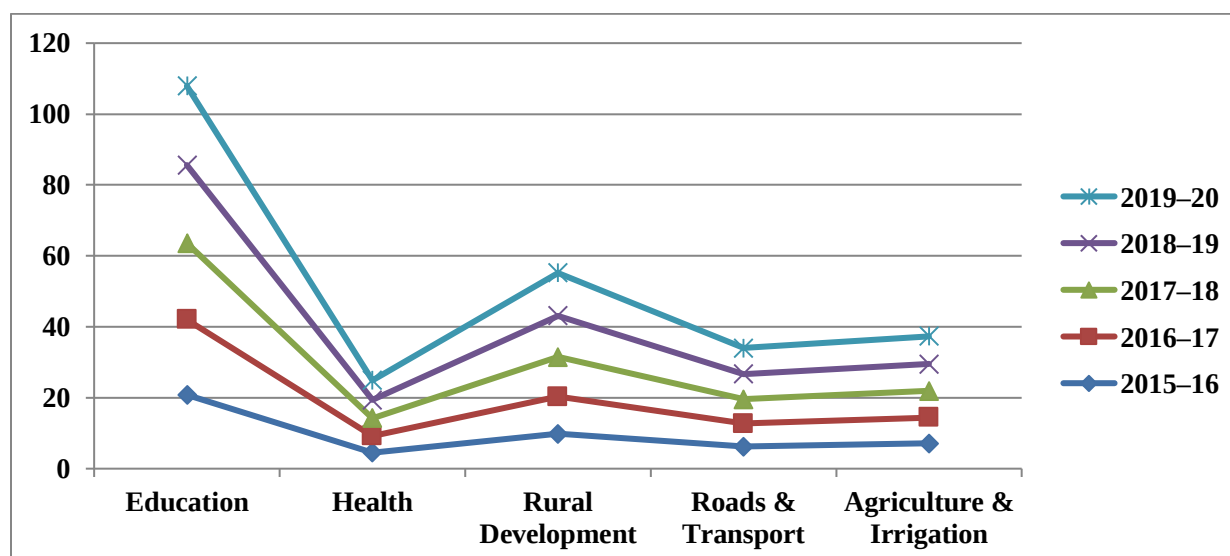
Fig. 1: Fiscal Indicators of Bihar under the Fourteenth Finance Commission

Sectoral allocations shown in Table 2 reveal that while education and rural development consistently received a significant share of resources, health spending remained below 6 percent of total expenditure. This reflects a persistent imbalance in Bihar's development strategy, where social infrastructure, particularly healthcare, has been underfunded relative to needs.

Table 2: Bihar – Sectoral Allocation of Expenditure (% of Total Expenditure, 2015–2020)

Year	Education	Health	Rural Development	Roads & Transport	Agriculture & Irrigation
2015–16	20.8	4.5	9.8	6.2	7.1
2016–17	21.2	4.7	10.5	6.5	7.3
2017–18	21.6	5.0	11.2	6.9	7.5
2018–19	22.0	5.2	11.6	7.1	7.6
2019–20	22.3	5.5	12.1	7.3	7.8

Source: Government of Bihar Budget Documents, Finance Accounts.


Fig.2: Trends in Sectoral Expenditure Allocation in Bihar

For comparative perspective, Table 3 contrasts Bihar with Odisha, another low-income state. While both states relied heavily on central transfers, Odisha exhibited stronger own-revenue effort and higher capital expenditure ratios, underscoring how governance capacity can influence developmental outcomes under the same fiscal framework.

Table 3: Bihar vs Odisha – Selected Fiscal Indicators (Average 2015–2020)

Indicator	Bihar (%)	Odisha (%)
Tax Devolution/Revenue Receipts	63.4	51.6

Own Tax Revenue/GSDP	6.7	8.5
Capital Expenditure/Total	13.4	16.8
Social & Economic Services Share	60.1	58.7

Source: RBI State Finances; Bihar and Odisha Finance Accounts.

To integrate fiscal data with analytical interpretation, Table 4 presents a SWOT analysis of Bihar under FC-XIV. It demonstrates that while decentralization expanded Bihar's fiscal opportunities, weak internal revenue mobilization, rising committed expenditure, and limited institutional strength continued to threaten the realization of development outcomes.

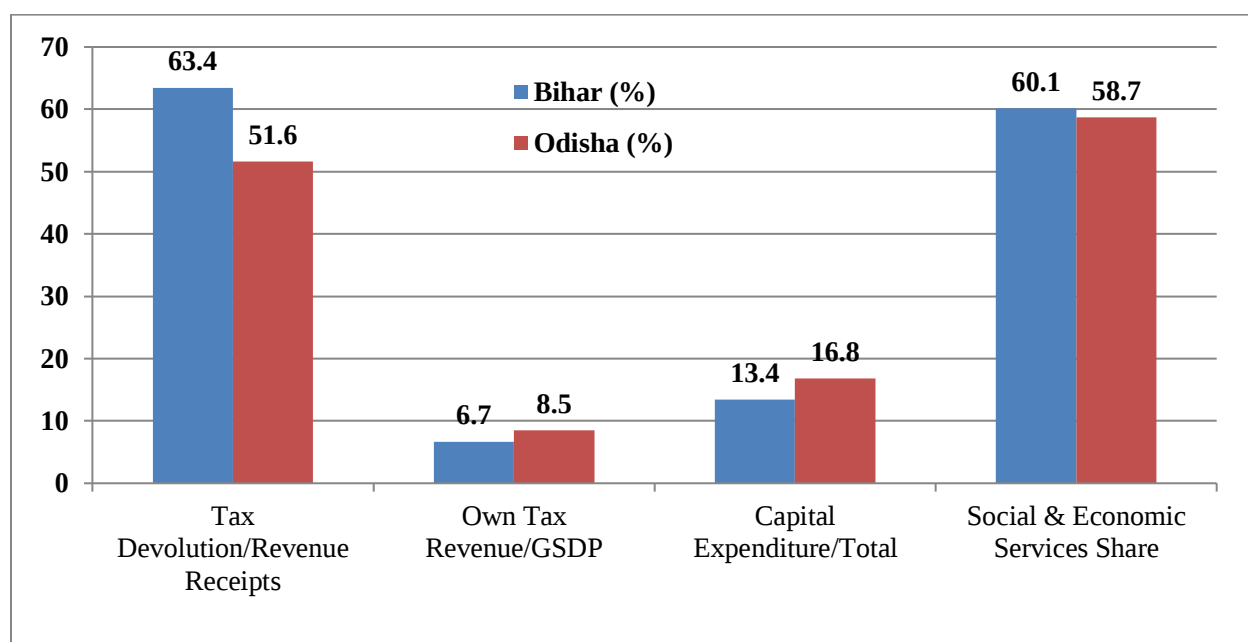


Fig.3: Comparative Fiscal Indicators of Bihar and Odisha

**Table 4: SWOT Analysis of Bihar under FC-XIV**

Strengths	Weaknesses	Opportunities	Threats
Largest-ever increase in untied transfers; predictable fiscal flows	Weak own-tax revenue effort; dependence on devolution	Ability to design state-specific programs; scope to expand capital investment	Rising committed expenditure; limited fiscal space for infrastructure
Higher allocation to social and economic sectors	Capacity constraints in PRIs and ULBs	Strengthening local bodies through predictable grants	Risk of inefficient utilization and leakages
Disaster relief fund flexibility (10% state-specific provision)	Delays in fund release and weak monitoring	Better disaster preparedness and relief planning	Continued vulnerability to floods and natural disasters

This analysis shows that while decentralization created an enabling fiscal framework for Bihar, the realization of developmental outcomes was contingent on internal reforms in revenue mobilization, expenditure efficiency, and local governance. The results thus present a nuanced picture: fiscal autonomy expanded considerably, but without complementary governance reforms, the developmental dividends remained modest.

5. Conclusion

The Fourteenth Finance Commission fundamentally reshaped India's fiscal federalism by enhancing the share of states in the divisible pool of central taxes. Bihar, as one of the most fiscally dependent states, experienced a significant expansion of untied resources during 2015–2020. This fiscal space enabled higher allocations to education, rural development, and welfare programmes, while predictable grants to local bodies and flexible disaster relief provisions



supported decentralized planning. However, the developmental dividends were constrained by structural and institutional weaknesses. Bihar's revenue effort remained among the lowest in the country, and a substantial portion of expenditure was absorbed by committed liabilities, limiting the potential for capital formation. Social sector spending rose but continued to be uneven, with health and infrastructure allocations remaining below requirements. Weak capacities of Panchayati Raj Institutions and Urban Local Bodies, along with delays in fund release and inadequate monitoring, restricted the effectiveness of decentralization. The state's experience illustrates that fiscal autonomy alone cannot guarantee development unless accompanied by stronger governance and financial management systems.

6. Policy Recommendations

To translate fiscal decentralization into sustained regional development, the following measures are suggested:

1. Strengthening Revenue Mobilization

- Expand the state's tax base through modernization of tax administration and rationalization of exemptions.
- Encourage greater efficiency in GST collection and improve compliance mechanisms.

2. Enhancing Capital Expenditure

- Protect capital outlays through medium-term fiscal frameworks and targeted fiscal rules.
- Prioritize infrastructure in transport, irrigation, and energy to generate long-term growth.

3. Balanced Social Sector Spending

- Increase allocations to the health sector, raising its share beyond the current 5–6 percent of total expenditure.
- Improve quality of spending in education by focusing on teacher training, infrastructure, and learning outcomes.



4. Empowering Local Governments

- Ensure timely release of grants to Panchayati Raj Institutions (PRIs) and Urban Local Bodies (ULBs).
- Introduce stronger accountability mechanisms through audits, participatory planning, and capacity-building programmes.

5. Strengthening Disaster Management

- Institutionalize district-level disaster planning, early warning systems, and rapid response mechanisms.
- Improve utilization of SDRF/NDRF funds to reduce delays in relief and rehabilitation.

6. Performance-linked Transfers

- Future Finance Commissions should complement devolution with incentives for states that demonstrate improvements in revenue mobilization, fiscal prudence, and efficiency in development spending.

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